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In the Supreme Court of the United States

OCTOBER TERM, 1934

GENERAL UTILITIES AND OPERATING COMPANY,
PETITIONER

v.

GUY T. HELVERING, COMMISSIONER OF INTERNAL REVENUE

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE FOURTH CIRCUIT

BRIEF FOR THE RESPONDENT IN OPPOSITION

INDEX

	Page
Opinions below	1
Jurisdiction	1
Question presented	2
Statutes involved	2
Statement	3
Argument	8
Conclusion	12

CITATIONS

Cases:

Burnet v. *Commonwealth Imp. Co.*, 287 U. S. 415	8
Commissioner v. *Owens*, 69 F. (2d) 597	9
Gregory v. *Helvering*, 293 U. S. 465	10
Hellebush v. *Commissioner*, 65 F. (2d) 902	10
Helvering v. *Rankin*, No. 582, October Term, 1934	11
Jones v. *Helvering*, 71 F. (2d) 214, certiorari denied, 293 U. S. 583	11
MacQueen Co., S. A., v. *Commissioner*, 67 F. (2d) 857	10
Phelps v. *Commissioner*, 54 F. (2d) 289	9
Phillips v. *Commissioner*, 283 U. S. 589	8
Prairie Oil & Gas Co. v. *Motter*, 66 F. (2d) 309	9
Seufert Bros. Co. v. *Lucas*, 44 F. (2d) 528	8
Story Parchment Co. v. *Paterson Co.*, 282 U. S. 555	8
Underwood v. *Commissioner*, 56 F. (2d) 67	8
United States v. *Phellis*, 257 U. S. 156	9
Virginia-Lincoln Furniture Corp. v. *Commissioner*, 56 F. (2d) 1028	8
West Texas Refining & D. Co. v. *Commissioner*, 68 F. (2d) 77	9

Statutes:

Revenue Act of 1928, c. 852, 45 Stat. 791:	
Section 111	2
Section 113	3

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No. 939

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v.

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OPINIONS BELOW

The opinion of the United States Board of Tax Appeals (R. 36–45) is reported in 29 B. T. A. 934. The opinion of the Circuit Court of Appeals (R. 62–72) is reported in 74 F. (2d) 972.

JURISDICTION

The judgment of the Circuit Court of Appeals was entered January 9, 1935 (R. 73). A petition for rehearing was filed February 6, 1935 (R. 75), and was denied April 2, 1935 (R. 134). Petition—

for a writ of certiorari was filed May 3, 1935. The jurisdiction of this Court is invoked under Section 240 (a) of the Judicial Code, as amended by the Act of February 13, 1925.

QUESTION PRESENTED

Whether the petitioner derived taxable profit on the sale of certain stock which it owned at the time the purchase price and general terms of the sale were agreed upon by the purchaser and the petitioner's president but which it distributed to its stockholders by way of dividend before the sale was consummated.

STATUTES INVOLVED

Revenue Act of 1928, c. 852, 45 Stat. 791:

> SEC. 111. DETERMINATION OF AMOUNT OF GAIN OR LOSS.
>
> (a) *Computation of gain or loss.*—Except as hereinafter provided in this section, the gain from the sale or other disposition of property shall be the excess of the amount realized therefrom over the basis provided in section 113, and the loss shall be the excess of such basis over the amount realized.
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> * * * * *
>
> (e) *Amount realized.*—The amount realized from the sale or other disposition of property shall be the sum of any money received plus the fair market value of the property (other than money) received.
>
> * * * * *

SEC. 113. BASIS FOR DETERMINING GAIN OR LOSS.

(a) *Property acquired after February 28, 1913.*—The basis for determining the gain or loss from the sale or other disposition of property acquired after February 28, 1913, shall be the cost of such property; * * *

* * * * * * *

STATEMENT

The following material facts are taken from the findings of the Board of Tax Appeals (R. 37–42), which were based upon a stipulation of the parties (R. 11–23):

The petitioner is a Delaware corporation, with its principal offices at Baltimore, Maryland. It is engaged in the business of owning securities of, managing, and operating public utility properties. On January 1, 1927, it acquired 20,000 shares of the common capital stock of another corporation, the Islands Edison Company, at a cost of $2,000. The said shares constituted one-half of the outstanding common stock of the Islands Edison Company, the remaining 20,000 shares being owned by Gillet & Company, which is not connected with the petitioner or its stockholders (R. 37).

During the month of January 1928 Walter Whetstone, president of the Southern Cities Utilities Company, became interested in acquiring control of a Santo Domingo company, the stock of which was owned by the Islands Edison Company. During a conference with J. C. M. Lucas, president of peti-

tioner, Whetstone discussed the purchase of the Santo Domingo Company or the Islands Edison Company common stock and as a result thereof was given permission to make an investigation of the properties of the Santo Domingo Company. Sometime in February of 1928 Whetstone informed Gillet and Lucas that his plans required the delivery of all the common stock of the Islands Edison Company, that he was informed by Gillet that his firm was ready and willing to make the sale of the 20,000 shares owned by Gillet & Company of the Islands Edison Company common stock, and that he (Gillet) and Lucas, president of petitioner, had agreed upon the price at which the sale would be made. Whetstone was informed by Lucas that if a sale of the 20,000 shares of the common stock of the Islands Edison Company then owned by the petitioner were consummated, such a sale would be made only after petitioner had distributed the Islands Edison Company shares to its stockholders, because they had been advised by their attorneys that if sale were made by petitioner it would be subject to a tax on any profit realized on the sale and that when the proceeds of the sale were distributed to the stockholders, the stockholders would have to pay another tax thereon. The price to be paid for the properties and the terms and conditions of the sale generally were agreed upon by Gillet, Lucas, and Whetstone, but no contract was entered into by them, it being understood and agreed between them that petitioner would make distribution of the

stock of the Islands Edison Company to its stockholders and that counsel would prepare a written agreement embodying the terms and conditions of the sale, the agreement to be submitted for approval to the stockholders of the Islands Edison Company after the distribution of said stock by the petitioner. Lucas never held power of attorney to sell the stock for the petitioner or its stockholders (R. 37–38).

At a meeting of the petitioner's directors on March 22, 1928, it was reported as the opinion of the petitioner's officers that the stock was worth at least $1,122,500. Resolutions were passed authorizing appreciation of petitioner's holdings on its books in the amount of $1,120,500 and declaring a dividend of $1,071,426.25 on the petitioner's common stock payable in stock of the Islands Edison Company at a valuation of $56.125 a share. On the same day the petitioner simultaneously made appropriate entries upon its books of account in compliance with this resolution (R. 38–39).

On March 22, 1928, in accordance with the resolution of the Directors, the petitioner distributed to its own stockholders 19,090 shares of the stock of the Islands Edison Company, such shares representing two shares of the Islands Edison Company stock theretofore owned by petitioner for each one share of the 9,545 shares of petitioner's own capital stock then outstanding. On the same date the shares of stock were transferred on the stock rec-

ords of the Islands Edison Company to the individuals receiving the distribution. After transfer of the 19,090 shares there remained in the hands of petitioner 910 shares of stock of the Islands Edison Company, which 910 shares were retained by it and a new certificate for such shares was issued to it on March 22, 1928 (R. 40).

On March 26, 1928, the stockholders of the Islands Edison Company (one of which was the petitioner, owning 910 shares) and the Southern Cities Utilities Company, entered into a written contract of sale of the Islands Edison Company stock. At no time did petitioner agree with Whetstone or the Southern Cities Utilities Company, verbally or in writing, to make sale to him or to the Southern Cities Utilities Company of any of said stock, except the 910 shares of the Islands Edison Company (R. 40).

The net consideration for the Islands Edison Company stock as computed in the contract of March 26, 1928, was $2,245,000, and this amount, divided by the number of shares (40,000), gives a quotient of $56.125 per share (R. 40–41). The 910 shares retained by the petitioner were sold to the Southern Cities Utilities Company on May 14, 1928, and a profit of $46,346.30 was reported on the petitioner's 1928 return, computed on a sale price of $51.25 per share less a cost of $0.10 per share. The difference between the amount of $56.125 per share, set forth as the price stated in the contract of

March 26, 1928, and the amount of $51.25, shown as the amount received on May 14, 1928, when the sale was made, is represented by brokerage charges, commissions, and other expenses incident to the consummation of the sale which were charged against the stockholders in accordance with the provisions of the contract. The petitioner received no cash or other property for the distribution of the 19,090 shares of the stock (R. 41).

The petitioner in making its income-tax return for the year 1928 reported no income from the disposition of the 19,090 shares of the Islands Edison Company common stock. Upon audit of the return the Commissioner held that petitioner derived a profit of $1,069,517.25 from the disposition thereof, giving as his explanation that this gain was realized upon distribution of the stock measured by the difference between the market value of $56.125 in satisfaction of a dividend obligation and the cost of $0.10 a share (R. 42).

The Board of Tax Appeals held that the declaration and payment of the dividend in stock resulted in no taxable income to the petitioner (R. 44–45). The Circuit Court of Appeals affirmed the Board's decision in this respect but held that the sale was in substance made by petitioner through its stockholders as agents or conduits through whom the transfer of title was effected, and reversed and remanded the case for further proceedings in accordance with its opinion (R. 71–72).

ARGUMENT

We submit that the court below was justified in holding that the petitioner is taxable on the gain represented by the difference between the sale price of the stock to the Southern Cities Utilities Company and its cost to the petitioner. The fact that the theory upon which the decision was based differed from that urged before the Board does not present a conflict requiring review by this Court. It may be conceded that some of the Circuit Courts of Appeals have declined to consider issues which were not raised before the Board of Tax Appeals, and that it is the practice of this Court that it will not consider issues not raised below. *Phillips* v. *Commissioner*, 283 U. S. 589, 605; *Burnett* v. *Commonwealth Imp. Co.*, 287 U. S. 415. But this is a rule of practice rather than a limitation of power. *Story Parchment Co.* v. *Paterson Co.*, 282 U. S. 555. The court below has reversed the Board on questions raised for the first time on appeal and has stated that it will not turn the taxpayer out of court because he may have misconceived his remedy. *Underwood v. Commissioner*, 56 F. (2d) 67 (C. C. A. 4th); *Virginia-Lincoln Furniture Corp.* v. *Commissioner*, 56 F. (2d) 1028, 1033 (C. C. A. 4th). The Government did not seek certiorari in those cases. And see *Seufert Bros. Co.* v. *Lucas*, 44 F. (2d) 528 (C. C. A. 9th).

This is not a case in which a corporation has distributed assets to its stockholders who thereafter find and sell to a purchaser. Here the stipulated

facts upon which the case was heard show that negotiations were commenced by the petitioner's president, and the purchase price and general terms of the sale were agreed upon before the stockholders had any right or title to the stock (R. 12–13, 38). The purchaser's plans required delivery of all the stock and not a part thereof (R. 12, 37). Before distribution all arrangements, short of legally binding contracts, were made, and it was agreed that the petitioner would make distribution of the stock and that counsel would prepare a written agreement embodying the terms and conditions of the sale to be submitted for approval to the Islands Edison Company stockholders after distribution (R. 13, 38). Such contract was prepared and approved and all the stockholders joined in selling the stock (R. 19, 40), thus ratifying the arrangements theretofore made.

Where a plan of action exists the courts will view the whole rather than subdivide into independent steps. *Prairie Oil & Gas Co.* v. *Motter,* 66 F. (2d) 309, 311 (C. C. A. 10th); *West Texas Refining & D. Co.* v. *Commissioner,* 68 F. (2d) 77 (C. C. A. 10th); *Commissioner* v. *Owens,* 69 F. (2d) 597 (C. C. A. 5th). Moreover, in matters of taxation the substance rather than the form of a transaction will be regarded. *United States* v. *Phellis,* 257 U. S. 156; *Phelps* v. *Commissioner,* 54 F. (2d) 289 (C. C. A. 7th). In substance there was one whole plan contemplated from its inception, and although the stockholders of the petitioner each

received title to a portion of the property this was but one step in carrying out a plan which was in essence a sale of the whole block owned by the petitioner through the instrumentality of its stockholders. In somewhat analogous circumstances the courts, viewing the whole transaction, have been guided by the substance rather than the form the transaction was permitted to follow. Cf. *Hellebush* v. *Commissioner,* 65 F. (2d) 902, 904 (C. C. A. 6th); *S. A. MacQueen Co.* v. *Commissioner,* 67 F. (2d) 857, 858 (C. C. A. 3rd).

Conceding the legal right of a taxpayer to avoid what would otherwise be his taxes by means which the law permits, as petitioner urges, nevertheless this principle, we submit, does not prevent the court from viewing a transaction as a whole or from recognizing its realities. The language used in *Gregory* v. *Helvering,* 293 U. S. 465, is pertinent. There this Court said (p. 469) that the proceeding was:

> Simply an operation having no business or corporate purpose—a mere device which put on the form of a corporate reorganization as a disguise for concealing its real character, and the sole object and accomplishment of which was the consummation of a preconceived plan, not to reorganize a business or any part of a business, but to transfer a parcel of corporate shares to the petitioner. No doubt, a new and valid corporation was created. But that corporation was nothing more than a contrivance to the end last

described. It was brought into existence for no other purpose; it performed, as it was intended from the beginning it should perform, no other function.

The decision is not in conflict with that of the United States Court of Appeals of the District of Columbia in *Jones* v. *Helvering,* 71 F. (2d) 214, certiorari denied, 293 U. S. 583, in which the facts and question presented were substantially different. There it was held that sales made for adequate consideration were none the less valid for tax purposes although the sellers owned a controlling stock interest in the purchaser and could have sold at a fictitious price. Nor is there a conflict, we submit, with *Helvering* v. *Rankin,* No. 582, October Term, 1934, decided by this Court April 29, 1935. In that case the court below departed from the facts found by the Board of Tax Appeals and assumed the existence of facts inconsistent with those found, and this Court held that it was not within the province of the court to make such findings. Here all the facts were stipulated, and on such stipulated facts the court determined that in substance there was a sale by the petitioner through the instrumentality of its stockholders.

Petitioner urges (Pet. 8) that the decision assigns a selling price of $56.125, whereas the basis was only $51.25. The actual selling price was $56.125 per share (R. 19). It is not clear from the stipulation (R. 19–20) whether all of the brokerage charges and commissions were absorbed by the

petitioner on its sale direct of 910 shares or whether such charges and commissions amounted to the sum of $4,875 on each of the 20,000 shares sold which had been owned by the petitioner. In any event, the court did not attempt to determine the amount of taxable gain but remanded the case for further proceedings. In such proceedings the amount of taxable gain may be determined.

CONCLUSION

The case depends largely upon its own facts, and upon those facts as stipulated the court below reached the correct result. There is no conflict of decisions requiring a review by this Court. The petition should be denied.

Respectfully submitted,

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